108TH CONGRESS
2nd Session

HOUSE OF REPRESENTATIVES

COMMITTEE PRINT

VIEWS AND ESTIMATES OF THE COMMITTEE ON FINANCIAL SERVICES ON MATTERS TO BE SET FORTH IN THE CONCURRENT RESOLUTION ON THE BUDGET FOR FISCAL YEAR 2005

FEBRUARY ___, 2004. Approved by the Committee on Financial Services.

Mr. OXLEY, from the Committee on Financial Services, submitted to the Committee on the Budget the following

R E P O R T

[together with

___________ VIEWS]

Pursuant to clause 4(f) of rule X of the Rules of the House of Representatives for the 108th Congress and section 301(d) of the Congressional Budget Act of 1974, the Committee on Financial Services is transmitting herewith (1) its views and estimates on all matters within its jurisdiction or functions to be set forth in the concurrent resolution on the budget for fiscal year 2005 and (2) an estimate of the budgetary impact of all legislation which the Committee expects to consider during the coming session.

OVERVIEW

The world is a very different place than the last time this Committee sat down to map out its budget priorities. The Nation is at war, and the threat from terrorism persists. The economy is rebounding from a shallow recession and many economists believe that the major economic indicators point to a strengthening economy.

However, much of this economic progress is threatened by growing deficits. The Administration projects a deficit of more than $500 billion for fiscal year 2005 and asks that the Congress do its part to reduce the deficit by half in the coming 5 fiscal years. This is no small feat given the budgetary demands of the war in Iraq and against terrorism, the need to improve the Nation's infrastructure, and providing assistance to those in need.

Despite the challenges, the Committee believes that reducing the deficit is an important priority. Continued deficit spending can have long-term effects on the economy. Higher deficits can lead to higher interest rates for businesses and consumers, resulting in reduced investment in equipment and human capital, lower consumer spending, and depressing the economic recovery. Further, increased interest rates can push the dream of homeownership out of reach for many Americans. Given the importance of the recent growth in the housing market in blunting the effects of the recession, it is important to keep that sector of the economy strong.

Deficits cannot be resolved by spending cuts alone. While reducing government outlays is an important part of the equation, fostering a robust economy that generates revenue to the Treasury is equally important. In order to foster the kind of growth that will lead the Nation away from deficit spending and into more secure budgets, it is essential that businesses and consumers have confidence in our markets and the basics of the economy.

The Committee has spent much of the past two years reinforcing the institutions which can bring back confidence to our markets. From passage of the landmark Sarbanes-Oxley Act in 2002, which fundamentally restructured the responsibilities of corporations to their shareholders, to last year's enactment of the Fair and Accurate Credit Transactions Act (FACT Act), which ensures that consumers have easy access to the information in their credit files and the tools needed to fight identity theft, the Committee has acted to improve confidence in all of the sectors of the economy. Similarly, the House also recently passed legislation authored in this Committee to bring back accountability to the mutual fund industry, so as to reassure investors that savings and investment is a prudent course of action.

The Committee is pleased to see that the President's budget continues important investments in the safety and soundness of our financial markets, such as the increased funding for the Securities and Exchange Commission (SEC) to protect investors, and commits to improvements in the regulatory apparatus which oversees important sectors of the economy, such as the proposal for a new regulator for the government sponsored enterprises of Fannie Mae and Freddie

Mac. Similarly, the President's budget reinforces the Administration's continuing commitment to fostering homeownership, through the newly funded FHA zero-down payment program, among other programs.

Just as last year, the Committee's legislative and oversight agenda will emphasize the need to improve investor confidence in our regulatory and market institutions, while recognizing the Nation's current fiscal situation, and the need to reduce the deficit for the long-term stability of the economy. However, by improving investor confidence in our markets, reducing transaction costs for businesses and consumers, and leveraging Federal investments in key sectors of the economy, such as housing, the Committee believes that the economy will grow, the recovery will continue, and the deficit will be reduced.

Details of the Committee's views and estimates on the fiscal year 2005 concurrent resolution on the budget follow.

SECURITIES AND EXCHANGE COMMISSION

One of the Committee's highest priorities in recent years has been to restore and promote investor confidence, a necessary component of a strong economy. The importance of the Securities and Exchange Commission in achieving that goal cannot be understated. The corporate scandals of recent years have underscored the need for effective and rigorous corporate governance. The Sarbanes-Oxley Act has already achieved much success in comprehensively changing attitudes both inside and outside the boardroom to ensure greater protection of investors and more efficient, competitive markets. That legislation empowered the Commission through enhanced administrative and budgetary authority. The enhanced budget authority that the President has proposed for the Commission will enable the Commission to continue its effective implementation of the provisions contained in the Sarbanes-Oxley Act, as well as its continued oversight of the new Public Company Accounting Oversight Board.

The Committee commends the President for his commitment to fund the needs of the SEC, and strongly supports the President's FY 2005 Budget to provide the SEC with $893 million, an $81 million increase over the 2004 level. The Committee lauds the President for providing the SEC with the greatest increase in its budget over the last 4 years compared to any previous administration. Since 2000, the SEC's budget has increased 243 percent. This commitment to America's investing public helps strengthen our capital markets, create jobs, and grow the economy.

In recent months, the confidence of the investing public has been shaken by rampant scandals in the mutual fund industry. The Committee, and the House of Representatives, took prompt action in passing H.R. 2420, the Mutual Funds Integrity and Fee Transparency Act, to ensure investors that their interests would be guarded by stronger independent boards of trustees, greater transparency of potential conflicts of interest, fund business practices and fees, and sensible regulations designed to prevent and punish those who engage in illegal market timing and late trading activities. Mutual funds have brought the benefits of professional management, portfolio diversification, and securities ownership to ninety-five million individuals. Mutual fund investors should be the direct beneficiaries of greater fee-based competition among mutual funds, more accessible and understandable information about mutual fund fees, stronger oversight by independent fund directors, and enhanced firewalls against a variety of conflicts of interest raised by the way mutual funds are operated and sold. H.R. 2420 would provide all of these reforms and should be enacted to protect the nation's current and future mutual fund investors. Passage of this legislation will place even more responsibilities on the SEC. While the SEC has proposed rules to implement many of the provisions for mutual fund reform laid out in H.R. 2420, additional rulemaking and enforcement will be necessary to fully comply with the directives contained in this important legislation.

GOVERNMENT SPONSORED ENTERPRISES

The Committee supports the President's call for improved regulation of the housing Government-Sponsored Enterprises (GSEs), Fannie Mae and Freddie Mac. The Committee is concerned that the current safety and soundness regulator, the Office of Federal Housing Enterprise Oversight (OFHEO), does not have sufficient resources, authority, financing, or staff to adequately monitor the activities of these large and complex institutions. This became clear to the Committee following the announcement that Freddie Mac would release three of its top executives, including the CEO, due to efforts to manage earnings. Since the announcement by Freddie Mac, OFHEO has done a commendable job of investigating the activities at Freddie Mac, imposing fines and penalties for the behavior in question, and recommending improvements in the corporate governance of the enterprises. However, the Committee believes that these problems at Freddie Mac could have been avoided and should have been investigated at the first sign of trouble. The Securities and Exchange Commission and the U.S. Attorney for the Eastern District of Virginia continue to investigate the activities at Freddie Mac.

The housing GSEs play an important role in providing liquidity to the secondary mortgage market. However, the size and influence of the GSEs on the national economy require that they be supervised by a regulator that has the tools to ensure the safety of the housing and financial markets. Fannie Mae, the Federal Home Loan Bank System, and Freddie Mac rank as the 2nd, 3rd, and 5th largest financial institutions in the United States respectively. The GSEs have outstanding debt obligations in the trillions of dollars and this debt is held by a large number of banking institutions, as well as domestic and international governments.

Oversight of Fannie Mae and Freddie Mac can be improved both with respect to the safety and soundness of their operations and with respect to their fulfillment of their housing mission. While it is important to recognize the unique operations of these GSEs, it is equally as important to recognize that they are all involved in sophisticated derivatives transactions and other complex financial dealings. The oversight of these transactions should be monitored by a regulator with the expertise and authority to ensure the safety and soundness of the enterprises.

The Committee looks forward to working closely with the Administration to craft a regulatory structure for the GSEs that promotes housing while protecting the national economy and the U.S. taxpayers. The Committee agrees that funding for a new regulator should continue to come through assessments on the GSEs and should be moved outside of the appropriations process. The Committee also agrees with the Administration that housing mission-related oversight of the GSE's should also be funded by assessments on the GSEs in order to improve the quality and rigor of that oversight.

The Committee also notes a growing interest among the Administration, relevant Senators, and some members of this Committee that regulation of the Federal Home Loan Banks (FHLBs) should be consolidated with the new regulator of Fannie Mae and Freddie Mac. While the FHLBs are unique in their ownership structure, there are many similarities between their operations and those of Fannie Mae and Freddie Mac. As the Committee continues its consideration of proposals to improve the regulation of the GSEs, it will carefully consider all of the proposals, including whether a unified regulatory structure for these entities will yield the desired improvements in safety and soundness regulation.

Terrorism Risk Insurance

During the 107th Congress, the Committee responded to the September 11 terrorist attacks by passing the Terrorism Risk Insurance Act (TRIA). This temporary program, administered by the Department of the Treasury, is scheduled to sunset on December 31, 2005.

Given TRIA's planned expiration, the Committee finds that the increased budget allocation for the program's general administrative costs warrants closer examination.

UNITES STATES MINT AND THE BUREAU OF ENGRAVING AND PRINTING

The President's budget message contains a proposal to study the advisability of combining the Department of Treasury's two money-manufacturing bureaus, the Bureau of Engraving and Printing (BEP) and the United States Mint (Mint). While the Committee understands and applauds the stated goal—achieving cost savings through reduction of administrative costs—and understands that on the surface this proposal may appear appealingly simple, the Committee will need to study the proposal further to determine if it is in fact cost effective.

The Committee notes that for good historical reasons the cultures and products of the Bureau and the Mint are different, as are their geographic locations, the nature of their workforces, and the mixture of unions representing those workforces. Furthermore, the distribution system and the budgetary accounting protocols for the two bureaus are entirely separate, and changes could lead to inadvertent budgetary effects. For instance, in the case of the BEP, the Federal Reserve is the issuer of its products, which are counterweighted by Treasury securities held in a portfolio that pays dividends to the Treasury. In contrast, the Treasury is the issuer of the Mint's coins, with no counterweight and after-production-cost funds deposited directly, but not scored, in the General Fund to avoid borrowing.

The Committee is aware of an ongoing study regarding the further privatization of some of the Mint's manufacturing options, which is due to be completed before the end of the year. The results of this study may fundamentally change the underlying assumptions regarding the cost of the Mint's operations, and thusit may be premature to contemplate the merger of these two agencies before the results of that study are known.

The Committee further notes concerns regarding internal control issues at the Mint raised by the Office of Inspector General and the General Accounting Office (GAO). The Committee also notes the long shutdown of the Mint's Philadelphia facility due to Occupational of Safety and Health Administration (OSHA) violations. While the current Director has made strides towards addressing many of these issues, the Committee will need to evaluate any proposal for combining the two agencies in light of progress on existing problems.

Finally, any examination of whether the merger of these two agencies is prudent must include a review of whether the Department of the Treasury should continue to administer this function, or whether it should be given to the Federal Reserve, as many other countries have consolidated monetary manufacturing and distribution systems.

The Committee does plan to examine two potential areas of cost savings for the Mint and BEP. First, both the Mint and BEP maintain their own separate security forces. Given the ongoing mission of the Secret Service to prevent the counterfeiting of U.S. coins and currency and to provide perimeter security at the White House and Department of the Treasury, consolidating these forces into the existing structure of the Secret Service may yield savings to the taxpayer, while improving the security of our currency production operations.

Second, the Committee is aware of recent reports of the Treasury Department's Inspector General which were critical of the Mint's leasing of new office space in downtown Washington. The Committee will work with the appropriate oversight authorities to ensure that both the BEP and Mint use their current real estate assets efficiently.

UNITED STATES SECRET SERVICE

The Committee notes with dismay that the budget message contains no new funding for the United States Secret Service's Electronic Crimes Task Force. While the Committee is not the authorizer for the Department of Homeland Security, it has a direct interest in the success of the electronic crimes task forces and believes an expansion of the program would be a direct benefit to all financial-services sectors under Committee jurisdiction. The regional task forces are a model of public-private cooperation, melding Federal, State and local law enforcement, academia, the private sector, and various non-governmental organizations that have interlocking interests in preventing a variety of crimes facilitated by computers and telecommunications, with the crimes ranging from child abuse to identity theft, credit care and related fraud, money laundering and terrorist financing. Given the success of the task forces at trust-building between these often-estranged groups, and in the speeding-up—or in some cases the initiation—of information flow leading to crime prevention or solving, the extraordinary leveraging of small amounts of funding for equipment and training cannot be overstated. The Committee views the task forces as important tools to protect the safety and soundness of the financial services sector and urges an expansion of funding.

The Committee also notes that the budget message for the Secret Service contains no specific budget item for expansion of overseas liaisons with foreign governments and foreign law enforcement with the specific mission of preventing the counterfeiting of currency and other security documents, including passports, identification cards, tax excise stamps, shipping manifests and bills of lading, etc. The Committee strongly believes that the Service does an exemplary job of suppressing counterfeiting at home and of working with other countries' governments and law enforcement to prevent the counterfeiting of U.S. currency and security documents abroad, funding this from regular budget lines. However, the Committee believes that especially in a time of increased terrorism and rapid globalization of financial markets, a small and specific investment in manpower and supplies is of utmost importance. Developing countries often lack the technical expertise to write, pass, implement, and enforce adequate laws against such activities, and in the cases where the Service has been able to invest even a single agent in a country liaising through its nearest large foreign field office, the results often have been dramatic. Given the increased need to know with certainty the true identity of the originator and recipient of financial transactions, and given the potential to fund terror acts with the proceeds of counterfeiting U.S. or other currencies, the Committee feels that identifiable, ongoing funding for this specific purpose is vital. Concurrently, the Committee notes the success of the Service's foreign field office program, particularly in South America and in South-Central Europe, and urges increased funding for expansion or new field offices, particularly in southern and western South America and in the Balkans. The Committee feels that these investments would help leverage other budget priorities at a minimal cost.

MILLENNIUM CHALLENGE ACCOUNT

On January 23, 2004, the President signed into law the Consolidated Appropriations Act (Public Law No. 108-199) which, among other things, authorized the Millennium Challenge Account (MCA). The MCA fosters innovation in development assistance to poor countries by seeking to assure accountability and measurable results. The funds in the Millennium Challenge Account will be distributed to developing countries that demonstrate a strong commitment toward good governance, the health and education of their people, and sound economic policies that foster enterprise and entrepreneurship.

The MCA will be headed by a Cabinet-level board of directors, including the Secretary of the Treasury. The Committee continues to have an oversight role over the MCA, since the Committee has jurisdiction over the international activities of the Department of the Treasury. The Committee also has an interest in encouraging consistent development assistance policies. The Financial Services Subcommittee on Domestic and International Monetary Policy, Trade, and Technology conducted a hearing on the MCA on June 11, 2003.

The Committee strongly supports the Administration's request for a substantial increase in funding for the MCA. The MCA, when combined with other multilateral assistance programs, sends a message of solidarity with the rest of the world in the fight to alleviate poverty and create better living conditions among countries that need that support the most. Finally, the Committee notes with favor that the funding request for the MCA initiative comes in addition to a requested increase in most existing core development accounts.

DEBT RELIEF

The Committee commends the President's request to provide an additional $75 million for the Trust Fund for the Highly Indebted Poor Countries (HIPC). This request fulfills the remaining portion of the U.S. pledge of $150 million to help meet the needs of the HIPC Trust Fund. These funds are consistent with the President's commitment made at the G-8 Summit in Kananaskis, Canada to contribute to the U.S. share of the projected HIPC Trust Fund financing gap. The Committee views multilateral debt relief as necessary to promoting the long-term debt sustainability of developing countries. The Committee has also requested the GAO examine different ways to measure debt relief. The Committee is looking forward to the completion of this GAO study in the near future and to continued oversight activities on debt relief issues.

WORLD BANK TRUSTEE ROLE IN THE GLOBAL FUND TO FIGHT AIDS, TUBERCULOSIS, AND MALARIA

The Global AIDS and Tuberculosis Relief Act of 2000, which was authored by the former Committee on Banking and Financial Services, was signed into law (Public Law 106-264) in August 2000. This legislation supports the creation of a World Bank AIDS Trust Fund. These initial steps by Congress were instrumental in establishing the Global Fund to Fight AIDS, Tuberculosis, and Malaria (Global Fund). Section 10 of the Framework Document for the Global Fund establishes the World Bank, an agency within the jurisdiction of the Committee on Financial Services, as the trustee for the Fund. The Committee looks forward to continuing its oversight over the World Bank's role as the Trustee for the Fund. The Committee also wants to continue to work with the Administration to maintain the effectiveness and accountability of the Global Fund.

The Committee notes with favor the Administration's funding requests for this trust fund. Although the amount is below the appropriated level for the last two fiscal years, the Committee notes the New York Times observation that this funding still represents "a big leap" in funding for global or international anti-AIDS programs compared to funding commitments in the last decade. The Committee believes that other aspects of the proposed budget underscore the Administration's continued commitment to fighting AIDS and believes these additional resources should be taken into account when assessing the United States' commitment to fight AIDS and other infectious diseases at the global level. For example, the World Bank's concessional lending window (the International Development Association) has committed to direct 18 percent to 21 percent of IDA lending to anti-AIDS programs and natural disaster reconstruction. The Administration is proposing a $1 billion appropriation for IDA. The Committee also appreciates the Administration's request for a substantial increase in the bilateral international AIDS program to target HIV/AIDS in 14 hard hit countries, and recognizes that the MCA initiative will be able to provide additional money, in part through grants, to help support developing countries' anti-AIDS programs.

NORTH AMERICAN DEVELOPMENT BANK (NADBANK)

The President's budget for FY 2005 seeks congressional authorization to implement reforms agreed to by President Bush and President Fox in March 2002 regarding the NADBank. These reforms include allowing the NADBank to authorize grants and to expand the geographic area of operations in Mexico. This Committee completed consideration of H.R. 254 on February 13, 2003, which authorized the President to agree to these reforms regarding the NADBank. The House passed this legislation (H.R. 254) on February 26, 2003. The Senate has yet to act on this legislation.

EXPORT-IMPORT BANK OF THE UNITED STATES

In the 107th Congress, the Committee reauthorized the Export-Import Bank (Ex-Im) for 4 years (Public Law 107-189) and views this agency as an important tool in facilitating the export of U.S. goods to foreign markets, especially in light of export support provided by other export credit agencies abroad to companies that compete with American companies for business internationally. The authorization mandated, among other things, that Ex-Im increase its level of small business transactions and invest in technology improvements to improve the access to the Bank's products. The Committee supports the continued investment by the Ex-Im Bank in technology.

The Committee remains concerned over the inconsistent appropriations for the loan credit subsidy for Ex-Im. The credit subsidy is the predicted cost of Ex-Im's portfolio of lending and insurance products. The volatility in Ex-Im's appropriation requests for the last three years has been directly related to whether appropriated funds were used. For instance, in FY 2003, Ex-Im received an appropriation of $513 million for its credit subsidy. No appropriation for credit subsidies were needed in FY 2004 because of excessive carry over loan subsidies and funds from cancelled transactions during the prior year. For FY 2005, the Administration now is requesting $125.7 million in credit subsidy. This appropriation request is lower than anticipated need because carryovers continue from previous year loan subsidies and cancellations. The Committee questions whether the taypayer would be better served with more consistent appropriations and more solid usage projections from year to year.

FINANCIAL CRIMES ENFORCEMENT NETWORK AND OFFICE OF FOREIGN ASSETS CONTROL

The Committee commends the President for requesting an increase in the budget of the Financial Crimes Enforcement Network (FinCEN) of almost $8 million, or 12.7 percent, to $64.5 million, to maintain current service levels. The increase reflects the importance of the duties assigned to the Government's central clearinghouse for a broad array of information on both money laundering and terrorist financing, and the increased duties assigned the bureau in title III of the USA PATRIOT Act (Public Law 107-56).

The Committee particularly commends the budget's focus on maintaining and improving the "Gateway" program designed to enable local, State and Federal law enforcement officers better, faster access to the data FinCEN collects. Appropriately, the FY 2005 budget request emphasizes the goal of making the Gateway program the single contact point for all law enforcement with respect to financial crimes. In the Committee's view, the importance of increasing information flow on financial crimes, and of decreasing the time necessary to access and act upon such information, is vital to both preventing and to solving crimes with a financial component. The Committee also notes with approval the budget's continued attention, in a separate line item, to FinCEN's ongoing efforts to establish a program for registration of money-service businesses, such as wire transfer providers and other non-bank financial institutions.

The Committee also notes that the importance of FinCEN's mission in combating terrorism and financial crimes is so crucial that the need for resources and the wise use of those resources continues to be paramount, and will continue to examine whether the bureau needs more resources, or needs to use them differently. In particular, the Committee is concerned with what it views as an unduly tentative start to efforts to automate institutions' filings with FinCEN of reports required by the Bank Secrecy Act, and the equally fitful rollout of FinCEN's system of notifying institutions of the need for increased vigilance on particular individuals or organizations of interest to law enforcement because of suspected financial crimes, including terrorist financing. The Committee believes that to be useful in preventing or quickly solving crimes that have a financial component, the sharing of data needs to be secure, essentially seamless and instantaneous. The Committee has traditionally had an interest in minimizing the burden on financial institutions of filing such information, and believes the Patriot Act Compliance System (PACS) mandated by the USA PATRIOT Act could, if properly deployed, go a long way towards that end.

The Committee supports the modest 2 percent increase—to $22.3 million—for the Office of Foreign Assets Control (OFAC), representing no new initiatives and no added positions. The Committee will continue to monitor OFAC, which administers and enforces economic sanctions and embargoes against targeted foreign governments and foreign or domestic groups that pose a threat to national security, for any extra needs.

Finally, the Committee continues to study the organization of the remaining Treasury Department enforcement components in light of the transfer of a significant portion of Treasury's enforcement functions to the new Department of Homeland Security. The Committee notes the creation last year of a new Assistant Secretary for Intelligence and Analysis position to handle classified information related to financial crimes and terrorism, and the Treasury's statement that in the new budget year it will work to integrate that position with existing Treasury operations. The Committee continues to believe that the Department must make a more disciplined and comprehensive effort to reorganize and revitalize its enforcement efforts to make them more effective.

TREASURY INSPECTOR GENERAL

The Committee notes with dismay the near-level funding of the Office of Inspector General, with a proposed increase of just over $1.2 million, to $14.2 million. The increase is focused mainly on adding 13 full-time equivalent positions, which is a welcome but, in the Committee's view, insufficient number. The Committee believes that the work product of the Inspector General is useful not only to the Secretary of the Treasury but also to the Committee as it exercises its oversight of the Department. Given Treasury's role as the Nation's bursar as well as its roles in enforcing economic sanctions and embargoes and in compiling and analyzing data on financial crimes, the Committee believes that a healthy, independent inspector general operation is vital not only to efficient operation but to continued cost-control efforts. Additionally, the Committee believes that increasing the number of audit positions at the office would be useful to provide ongoing analysis of a variety of regulatory and compliance operations performed by the Department, including coordination between enforcement and regulatory functions and the reliability and usefulness of Bank Secrecy Act and similar data. In particular, as questions have been raised about the controls in and compliance with the Office of Foreign Assets Control in its fight against money laundering and terror financing, adequate resources to devote to a study of that subject are important. Given that a large portion of the Inspector General's office moved to the new Department of Homeland Security (DHS) and to the Department of Justice upon the formation of DHS, the Committee believes that the Treasury Inspector General's office remains under-funded.

FINANCIAL SERVICES REGULATORY RELIEF

The Committee expects to bring to the House floor this session H.R. 1375, the Financial Services Regulatory Relief Act, legislation giving banks, thrifts, and credit unions relief from outdated and unnecessary regulatory burdens, as a way of improving the productivity of the financial services sector and counter-balancing the significant regulatory burdens imposed upon depository institutions as part of the global effort to combat terrorist financing. The Committee favorably reported H.R. 1375 during the first session. The Congressional Budget Office estimated that enactment of H.R. 1375, as reported by the Committee, would reduce Federal revenues by a total of $117 million over the 2004-2013 period, and that direct spending would increase by a total of $22 million over the same period. The Committee expects to mitigate the direct spending increases identified by CBO prior to consideration of H.R. 1375 by the full House.

INTEREST ON STERILE RESERVES

Last session, the House passed by voice vote H.R. 758, the Business Checking Freedom Act of 2003, authorizing the Federal Reserve to pay interest on reserves that depository institutions are required to hold at Federal Reserve Banks against their customers' transaction accounts. The Senate has not taken up the legislation. For the reasons outlined below, the Committee expects that enactment of H.R. 758 would have little effect on the FY 2005 Federal budget.

Under the Federal Reserve Act, banks, thrifts, and credit unions are required to maintain reserves at Federal Reserve banks based on the volume of transaction accounts that they hold. Because the Federal Reserve pays no interest on such reserves, they have come to be known as “sterile reserves,” and depository institutions have developed techniques for minimizing their reserve requirements, chiefly through “sweep” programs that permit funds to be transferred out of reservable transaction accounts into non-reservable instruments, such as money market deposit accounts, at the end of each business day. As a result, reserve balances at the Federal Reserve banks have declined dramatically in recent years, falling from approximately $28 billion in 1993 to approximately $7 to 8 billion in 2002. According to the Federal Reserve, the precipitous decline in reserves has potentially adverse consequences for its ability to conduct effective monetary policy, and the Fed has therefore strongly supported legislation to permit it to pay interest on reserves.

CBO’s analysis of H.R. 758 concluded that the payment of interest on reserves would cost approximately $608 million over 5 years (FY 2004-2008). However, because the legislation offset this cost through 2007 by mandating the transfer of an equal amount of Federal Reserve surplus funds to the U.S. Treasury, CBO deemed the legislation to be effectively budget-neutral for the period 2004-2007. If budget offsets are not found for subsequent years, CBO estimated that the legislation would result in a loss of revenues for the period 2008-2013 of approximately $1.5 billion.

DEPOSIT INSURANCE REFORM

Last session, the House passed H.R. 522, the Federal Deposit Insurance Reform Act of 2003, by a vote of 411 to11. Although the Senate has not yet acted on deposit insurance reform, the Committee will continue to push for enactment of this important legislation, to ensure the continued vitality of a program that has promoted public confidence and stability in the nation’s banking system for the last 70 years.

H.R. 522 will preserve the value of customer deposits at insured depository institutions, advance the national priority of enhancing retirement security for all Americans, and guarantee that the value, benefit and costs of deposit insurance are allocated equitably and fairly across all depository institutions and their customers. The bill merges the Bank Insurance Fund (BIF) and the Savings Association Insurance Fund (SAIF); increases the deposit insurance coverage limit from $100,000 to $130,000, and indexes it every 5 years for inflation; doubles the new coverage level for certain retirement accounts; and gives the Federal Deposit Insurance Corporation (FDIC) greater discretion to administer the deposit insurance fund with more sensitivity to cyclical forces in the banking system and the economy as a whole.

In the 107th Congress, the House passed deposit insurance reform legislation substantially similar to H.R. 522 which the CBO estimated would *decrease* net Federal spending by $700 million. Yet in performing its analysis of H.R. 522, the CBO applied a different set of assumptions, and concluded that the legislation would *increase* net Federal spending by some $1.9 billion. CBO acknowledged the speculative nature of its estimate, stating that "it is possible that the FDIC could use its broad discretion [under H.R. 522] differently than we have assumed and that could result in either fewer or greater premium collections that CBO has estimated."

The FDIC has strongly challenged the CBO's assumption that the FDIC would not achieve revenue-neutrality in administering the deposit insurance fund under H.R. 522. In a March 31, 2003, letter to Chairman Oxley, FDIC Chairman Don Powell stated: "Because any analysis that determines H.R. 522 will result in an increase in net government spending must necessarily rely on assumptions regarding how the FDIC Board will exercise the discretion provided in the legislation, I can assure Congress that the leadership of the FDIC has no intention of managing the deposit insurance system in a way that increases cost to the government or increases the burden on insured institutions. The costs of the deposit insurance system will continue to be borne by the banking industry * * *." Consequently, the Committee disagrees with the CBO analysis and believes that the enactment of the legislation will have little budgetary impact.

HOUSING AND URBAN DEVELOPMENT BUDGET

The Administration proposes $31.3 billion in FY 2005 budget authority for the Department of Housing and Urban Development (HUD), representing a 2.8 percent increase. In releasing the President's budget, Acting Secretary Alphonso Jackson stated, "This budget will create new opportunities for families and individuals who seek affordable housing and the American dream of homeownership and will generate new stability and prosperity for the communities in which they live and work." This Committee is mindful that HUD faces many difficult management and budget challenges. Programs such as the Section 8 rental housing assistance now account for more than one-half of the HUD budget. In addition, some argue that many of the Nation's 1.25 million public housing units are in need of capital repair.

Over the past few years, this Committee and the current and past Administrations, have continued to seek bipartisan ways to make existing housing programs work better. As an example, in 2003, the Committee successfully enacted legislation through the American Dream Downpayment Act that would annually benefit approximately

45,000 new homeowners and families. At the same time, the Committee successfully enacted legislation to increase FHA multifamily loan limits, which addresses the acute issue of affordable rental housing in extremely high-cost areas. The combination of these two legislative efforts should provide momentum to assist new families and individuals that have been left out of the conventional housing and/or mortgage finance markets.

Again, the Committee is pleased that the Administration is proposing new initiatives to address acute homeownership and rental housing challenges. In meeting the President's homeownership agenda to increase minority homeownership by at least 5.5 million households, the Committee recognizes that a range of options are necessary, including: H.R. 3755, the Zero Downpayment Act of 2004, a potential housing counseling bill, as well as efforts suggested by the President through the tax code to implement a "Low-Income Housing Tax Credit." A combination of proposals could address the issue of a less than 50 percent homeownership rate among minority communities, as compared to a general homeownership rate of 68 percent.

While homeownership policy is the best avenue for strengthening families and improving communities, the Committee also recognizes that there is a sector of American society that is not yet ready or available to pursue homeownership. Therein is the conundrum of this Committee and other policy-makers: how to address a growing need for affordable rental housing in those regions of the country where it is purported that few if any housing units exist for working class or low-income families.

The Committee recognizes that there are several perspectives and approaches to create new rental housing opportunities. However, any new approach is handcuffed by the potential hemorrhaging of the Section 8 rental housing subsidy program that will eventually consume the entire budget of the Department of Housing and Urban Development, unless serious and dramatic reform is undertaken. This is a reality that this Committee has expressed in previous Committee Budget Views and Estimates. Without meaningful reform, the good work achieved by other housing programs, such as the Community Development Block Grant or Home Investment Partnerships Everywhere (HOME), would most likely evaporate.

In 2003, the Subcommittee on Housing and Community Opportunity held 17 housing hearings, with 5 specifically focused on the Section 8 rental housing subsidy program and another 9 hearings on affordable housing issues. At that time, housing experts and advocacy groups expressed concern about the President's proposal to block grant the rental subsidy program to State governments for their control and administration. While that proposal was not considered by this Committee, in its budget request, the Administration presents a new proposal that attempts to address the same program issues and concludes that a serious budget crisis is imminent.

Given the strident budgetary constraints, it is the Committee's responsibility to review all the proposals, including those of the Administration, to determine what course-of-action, if any, should be pursued. During this process, the Committee will balance the question of how to achieve reform that meets budgetary realities, that allows the program to work more efficiently, and that ensures assistance to working and/or low-income families.

In the first session of the 108th Congress, the Committee held numerous public hearings in order to understand and to educate the public about current housing issues. In the second session of the 108th Congress, the Committee expects to undertake similar hearings.

Zero Down Payment Mortgage. In his FY 2005 budget, the President proposed legislation to offer a new mortgage product to help first-time homebuyers purchase a home by allowing zero down payment loans and financing of the settlement costs. HUD estimates that this new FHA product will help an estimated 150,000 families a year purchase their first home. Legislation to implement this new program was introduced on February 3, 2004, by Representatives Tiberi and Scott (H.R. 3755, the Zero Down Payment Act of 2004). The Committee will hold hearings on this important initiative and looks forward to working with the Administration to see that this program is enacted.

American Dream Downpayment. The Committee is pleased that the Administration has again included funding for the American Dream Downpayment initiative. Last year, this Committee was instrumental in guiding this program to enactment. Clearly, this is a program that will help tens of thousands of low-income families a year to become first-time homeowners.

Housing Counseling. The Committee believes that counseling is an important component of the successful homeownership process and agrees with the President that it is important to help families learn about the loan products and services available to them. Being able to identify and avoid predatory lending practices is critical to increasing homeownership. Counseling has proven to be an extremely important element in both the purchase of a home and in helping homeowners keep their homes in times of financial stress. The Committee applauds the Administration's proposal to increase funding for housing counseling. The President's plan includes a record $45 million to support 550,000 families with home purchase and homeownership counseling and about 250,000 families with rental counseling. In the past three years, the Bush Administration has more than doubled funding to this program.

Section 8 Rental Housing Assistance Program. The Committee applauds the Administration for its continued efforts to find a solution to the long-standing concern with the Section 8 tenant-based voucher program. Over the past few years, Congress has grappled with issues regarding the overall cost of the program, underused vouchers, the allocation of vouchers for public housing authorities (PHAs) and the general management of the program. Last year, in its FY 2004 budget, the Administration proposed a different approach to address these long-standing concerns with the Section 8 tenant-based voucher program. “Housing Assistance for Needy” (HANF) would move this program to a State-run block grant model over a two year period while requiring each State to provide vouchers to at least the same number of families as currently receiving support. The Subcommittee held a series of hearings on this proposal, but no legislative action was taken regarding the Administration’s HANF proposal.

This year, the Administration proposes a different approach designed to address the dramatic increase in program costs. Instead of a block grant to the States, the Flexible Voucher Program (FVP) would change the current unit-based funding for the Housing Choice Voucher Program to a dollar-based grant program that will be administered by public housing authorities. The new FVP will allow public housing authorities (PHAs) to set rents using local rental market data. Proponents argue that giving local officials the authority to use local rental market data will stop the spiraling cost of the Housing Choice Voucher Program. The Administration believes that this new FVP program will lead to significant cost savings to the voucher program and will provide performance-based incentives for PHAs to serve more families presently waiting of rental assistance.

As part of the new Flexible Voucher Program, local housing agencies would be allowed to use rental assistance vouchers toward moving low-income families into homeownership. The housing agencies could either provide mortgage assistance in lieu of a rental subsidy or offer families a one-time down payment grant equaling up to one-year’s worth of their rental assistance. The Committee is cognizant of the fact that unless dramatic reform is undertaken, the Section 8 rental housing subsidy program will eventually consume the entire HUD budget. The Committee will review the Administration’s new proposals carefully as it contemplates how best to address this quandary, and looks forward to working with the Administration to find a solution to the budget and management challenges facing the Section 8 program

Public Housing. The President's budget includes $3.6 billion for the Public Housing Operating Fund to fund local housing authorities in their daily operation and $2.7 million for the Public Housing Capital Fund to help local housing authorities fund major repairs and modernizations in their housing units. Also, in FY 2005, up to $55 million will be available for the ROSS program, which provides supportive services and assistance to residents in becoming economically self-sufficient. HUD will introduce a demonstration program in 2005, Freedom to House: Public Housing Reform Demonstration Program designed to improve public housing. The Freedom to House Initiative will allow 50 PHAs the freedom to establish rents for their residents based on their local rental market, rather than on national rental estimates. Under this program, PHAs will also have the ability to combine their capital and operating funds. The Administration believes that this will allow PHAs to significantly cut their administrative costs which will allow them to service more families. This Committee is aware of the fact that the current rent setting mechanism does not allow PHAs the flexibility needed to meet the unique housing needs of their local communities. Furthermore, the Committee is equally concerned about the availability of decent, affordable housing for low-income families. Consequently, the Committee will carefully review the Administration's proposals as it determines how best to meet these important challenges.

HOPE VI. The Administration again proposes to discontinue funding for the HOPE VI program. The Committee understands that while the HOPE VI program has enjoyed many successes, the program has been plagued with accountability and management problems. Despite these challenges, each year the Committee on Appropriations continues to include funding for the HOPE VI program. Last year, this Committee considered and approved H.R. 1614, the HOPE VI Program Reauthorization and Small Community Main Street Rejuvenation and Housing Act of 2003. In addition to reauthorizing the program through September 30, 2005, H.R. 1614 includes provisions to allow 5 percent of HOPE VI funds for assistance to smaller communities in order to provide affordable low-income housing in connection with main street revitalization or redevelopment projects. In addition, H.R. 1614 includes several management changes to make the program more accountable and sensitive to the people it is intended to assist. H.R. 1614 was included in S. 811, the American Dream Downpayment Act which became Public Law 108-186. The Committee will continue to conduct oversight of the program to determine if other changes to the program are necessary and to monitor the implementation of the Small Community Main Street Rejuvenation program.

Self-Help Homeownership Opportunity Program (SHOP). The Committee fully supports the Self-Help Homeownership Opportunity (SHOP) Program and believes it is an important component of achieving the goal of producing new homes for very low-income families. The Committee supports President Bush's request for $65 million to fund so-called "sweat equity" homeownership programs to support nonprofit organizations such as Habitat for Humanity, which require low-income families to help construct the homes they will eventually own. These funds will help produce approximately 5,200 new affordable homes nationwide.

The Samaritan Initiative. The Committee applauds the Administration's goal of ending chronic homelessness and supports the $50 million in housing assistance for those experiencing chronic or long-term homelessness included in the President's FY 2005 Budget. The Committee will hold hearings and consider the Administration's proposal to combine HUD's permanent housing funding with assistance from the Departments of Health and Human Services (HHS) and Veterans Affairs (VA) for supportive services such as substance abuse treatment and primary health care.

Brownfields. The Committee notes with concern the elimination of funding for the Brownfields Economic Development Initiative (BEDI) and would like funding restored for the program. While the Environmental Protection Agency (EPA) administers programs to revitalize brownfields, HUD should not vacate its own role in cleaning up these blighted sites. HUD should follow through on its proposal in the FY 2003 budget to decouple the BEDI program from the Section 108 loan program to attract more participants. The BEDI program can be a powerful tool for communities interested in brownfields redevelopment. Fostering a partnership with the EPA will be helpful for both agencies and for the Nation's urban areas.

RESPA Reform. The Committee is committed to the Administration's goal of simplifying the home buying process and making it less expensive to consumers. The Committee will continue to monitor the progress of this rulemaking to ensure that it will be both fair and provide consumers with better opportunities to shop for low-cost mortgages. On December 17, HUD sent a final RESPA reform rule to OMB for consideration.

FEDERAL EMERGENCY MANAGEMENT AGENCY

The National Flood Insurance Program (NFIP) has been affected by two major developments in the last several years: a major internal realignment of flood insurance and mitigation, and the Federal Emergency Management Agency's (FEMA's) overall consolidation into the new Department of Homeland Security (DHS). In June 2001, FEMA underwent a major realignment designed to integrate better the functions that take place in the emergency management process: preparedness, mitigation, response, and recovery. The realignment combined the agency's mitigation functions and Federal insurance functions to form FEMA. FEMA underwrites issues and services insurance policies under the NFIP with assistance from private insurance companies and servicing contractors.

The NFIP is funded through premium dollars that are paid by the policyholders. However, the President's FY 2005 budget request does include a request for such items as salaries and expenses associated with flood mitigation and flood insurance operations and funds for flood hazard mitigation.

The President's FY 2005 budget includes $200 million for the Flood Map Modernization Fund. This fund is used to update and modernize the inventory of over 100,000 flood maps. Property owners are required to purchase national flood insurance if their properties are in the 100-year flood plain as determined by the flood maps.

The NFIP authorization is due to expire on June 31, 2004. In the first session of the 108th Congress, the House approved short-term program extensions while working on legislation to reauthorize and reform the National Flood Insurance Program. On July 23, 2003, the Committee completed their consideration of H.R. 253, the Flood Insurance Reform Act of 2003, which would extend the authorization of the NFIP through 2008 and would address the problem of repetitive loss properties (buildings that flood regularly because of their location) and the threat such properties pose to the ability of the NFIP to meet obligations to policyholders without drawing on taxpayer funds. Repetitive loss properties cost the NFIP approximately $200 million each year. 1 percent of all properties in the NFIP account for approximately 25 percent to 30 percent of all the NFIP losses. H.R. 253 passed the House on November 20, 2003 and is currently awaiting Senate action.

The Committee wishes to emphasize the importance of reforming this program. A series of short-term extensions will not protect the policyholders and taxpayers from ever-escalating costs. The Committee looks forward to sending legislation to the President reforming this program before the current authorization runs out at the end of June, 2004.

RURAL HOUSING SERVICE

The Rural Housing Service (RHS) faces a variety of management and budget challenges in both its single and multifamily housing programs. The Committee appreciates the Administration's efforts in the FY 2005 budget proposal to address those challenges. In the years to come, the growth in rural population and the predominance of low-wage jobs will translate into an increased need for affordable capital to fund housing and community facilities. Last year, the Committee held a series of hearings to determine how well the RHS is meeting the housing needs of rural America.

In 2005, the Rural Housing Service FY 2005 budget proposes a reduction in the USDA Rural Housing Service's Section 515 program from $116 million in FY 2004 to $60 million in FY 2005. USDA has a portfolio of about 17,800 existing multi-family projects with an outstanding indebtedness of about $12 billion. Most of these projects were built in the 1980s and are, or will soon be, eligible for prepayment and departure from the program. There are also concerns about the physical condition of existing projects and the ramifications of allowing projects to leave the program. In particular, some have raised concerns about the potential impact on existing tenants and other low-income people on the availability of affordable housing. No new construction would be supported in the FY 2005 budget. Instead, funds would be available only for repairs and rehabilitation of current projects. The Committee is pleased that USDA is conducting a thorough review of the matter and working to develop better strategies for managing the existing portfolio of projects before adding to future costs by funding new projects.

The Section 502 direct mortgage program would be cut slightly, from $1.4 billion in FY 2004 to $1.1 billion in FY 2005. Of particular note is the inclusion of an increase in the fee on guaranteed 502 loans. In October 2002, the one-time fee on guaranteed loans to purchase housing was reduced from 2 percent to 1.5 percent and to ½ percent for loans to refinance existing RHS loans. This action was taken as part of the President's initiative to increase homeownership, especially among minorities. This reduction resulted in a significant increase in demand. The FY 2005 budget reflects a partial offset, with the fee on new loans being increased from 1.5 percent to 1.75 percent. The Administration expects this change to reduce subsidy costs and to provide for a more manageable growth in the program. In addition, the budget proposes legislation to allow guaranteed loans to exceed 100 percent of appraised value by the amount of the fee on such loans. The administration believes this will help ensure that rural families are not denied home ownership for lack of funds to pay the cost of the fee.

The rural rental assistance program provides funding for multi-year contracts with project owners for reducing rent payments to make up the difference between the 30 percent of income the low-income tenant pays and the rent required for the project owner to meet debt-servicing requirements. Most of the funding for this program is used to renew expiring contracts on projects that are financed for up to 50 years although dependent on rental assistance that is funded in shorter-term increments. In developing the Consolidated Appropriations Bill for 2004, Congress decided to reduce the renewal cycle on rental assistance payment contracts from 5 years to 4 years. The 2005 budget continues this policy and the Committee agrees.

Most other USDA RHS programs would be funded at about the same levels as in 2004. The budget would eliminate USDA's capacity-building Rural Community Development Initiative, funded at $6 million in FY 2004. The Committee will continue to review the programs under the Rural Housing Service to determine what changes are necessary to address future budget and management challenges.

NEIGHBORHOOD REINVESTMENT CORPORATION

The Committee is pleased that the Administration has proposed a total of $115 million for the Neighborhood Reinvestment Corporation (NRC) including $5 million for a multi-family rental-housing. This funding level will allow the NRC to continue its mission "to revitalize older urban neighborhoods by mobilizing public, private, and community resources at the neighborhood level."